No. 80-264

IN THE

Supreme Court of the United States

October Term, 1980

ELMER B. STAATS, COMPTROLLER GENERAL OF THE UNITED STATES,

AND

UNITED STATES OF AMERICA,
Petitioners,

v.

BRISTOL LABORATORIES DIVISION OF BRISTOL-MYERS COMPANY,
Respondent.

ON WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE SECOND CIRCUIT

BRIEF OF MERCK & CO., INC. AND SMITHKLINE CORPORATION, *AMICI CURIAE*

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BRIEF OF MERCK & CO., INC. AND SMITHKLINE CORPORATION, *AMICI CURIAE*

Merck & Co., Inc. ("Merck") and SmithKline Corporation ("SmithKline") submit this brief as *amici curiae* in support of the judgment of the Second Circuit.

INTEREST OF AMICI CURIAE

1. The *Amici* and Respondent are Similarly Situated.

The *amici curiae* SmithKline and Merck, like respondent Bristol Laboratories Division of Bristol-Myers Company ("Bristol"), are leading pharmaceutical manufacturers. In August

1974, Bristol, Merck, SmithKline and three other pharmaceutical companies were served by the Comptroller General with identical demand letters seeking access to their records relating to a handful of government procurement contracts.[1] In each instance, the Comptroller General's demand was premised on identical standard form access-to-records provisions inserted in their contracts pursuant to 10 U.S.C. § 2313(b) and 41 U.S.C. § 254(c).

Although those statutes and the relevant contractual provisions restrict the Comptroller General to records that are "directly pertinent to" and involve "transactions relating to" the specific procurement contract, the letters served on the *amici* and Bristol made sweeping demands for access to virtually all the records of these companies.[2] The broad scope of the access demands is evident from the government's acknowledgement that GAO is seeking to inspect records of "all costs met in whole or in part from revenues earned on the federal contracts" listed in the demand letters. Pet. Br. 7, *quoting* Pet. App. 9a. As the District Court found in this case:

> "The Government's theory has far reaching implications. The only items excludable from the Comptroller General's reach would be those, if any, which related to costs recovered exclusively from non-government contracts. *** It is undisputed, however, that Bristol does not separately compute the cost of government and non-government contracts or pay for them out of separate funds. Accordingly, *there are no excludable records under*

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[1] *See* Joint Appendix ("J.A.") 20-21; Joint Appendix filed in the court of appeals in *Merck & Co. Inc.* v. *Staats*, D.C. Cir. Nos. 79-1435 & 74-1438 (argued Feb. 11, 1980)("Merck C.A. App.") 49-51; Joint Appendix filed in the court of appeals in *SmithKline Corporation* v. *Staats*, 3d Cir. No. 1464 (filed March 19, 1980)("SmithKline C.A. App.") 60-63. Copies of the joint appendices in the *Merck* and *SmithKline* cases have been lodged with the clerk of this Court.

[2] The Comptroller General's letters demanded access to records "which include but are not limited to (1) records of experienced costs including costs of direct materials, direct labor, overhead, and other pertinent corporate cost, (2) support for prices charged to the Government, and (3) such other information as may be necessary for use to review the reasonableness of the contract prices and the adequacy of the protection afforded the Government interests." J.A. 21; Merck C.A. App. 50; SmithKline C.A. App. 61.

the Government's theory." 428 F. Supp. 1388, 1390 (Pet. App. 9a)(emphasis added).

Like Bristol, both Merck and SmithKline divide their costs into a category of direct manufacturing costs assignable to particular products and another category of unassigned costs, including all research and development, marketing, distribution, advertising and general administrative costs. This common practice reflects the fact that there are no generally accepted accounting principles which permit the accurate and meaningful allocation of the latter category of costs to particular products.[3] Since Merck and SmithKline do not assign costs to particular contracts and do not segregate revenues generated by particular contracts, the interpretation of the access-to-records statute asserted here by the government would encompass *all* of the *amici's* cost records. Indeed, the drastic reach of the identical access demands served on Bristol and the *amici* is illustrated by GAO's expressed inability to define any category of records that would fall outside its demands.[4]

Faced with these sweeping demands, Merck and SmithKline, like Bristol, declined to produce records sought by the Comptroller General and initiated actions seeking declaratory and injunctive relief.[5] The cases initiated by Merck and

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[3] *See* Merck C.A. App. 97; SmithKline C.A. App. 377-92. Petitioner Staats has acknowledged that it would be impossible to ascertain what these pharmaceutical companies' costs are with respect to individual drug items. *See* pp. 25-26 *infra*.

[4] *See* Merck C.A. App. 156, 346-47. Not only has the government failed to identify categories of records that would fall outside its access demand, but GAO has indicated in response to discovery taken in the *Merck* case that it may demand access to records dating back *20 years* or more prior to the date on which the contracts were awarded. *Id.* This testimony is reprinted in Appendix B, *infra*, pp. 5a-6a.

[5] Merck filed suit in the United States District Court for the District of Columbia, *Merck & Co.* v. *Staats*, Civ. Action No. 74-1447 (D.D.C. 1977), *cross-appeals pending*, D.C. Cir. Nos. 79-1435, 79-1438 (argued Feb. 11, 1980), *conditional petition for certiorari before judgment denied*, No. 80-416 (Dec. 8, 1980). SmithKline brought its action in the United States District Court for the Eastern District of Pennsylvania, *SmithKline Corporation* v.

(footnote continues)

SmithKline are presently pending in the District of Columbia Circuit and the Third Circuit, respectively. Given the common origin of the cases brought by these three companies and the important common question of statutory construction they raise, SmithKline and Merck clearly have a direct and substantial interest in this Court's resolution of the issue presented here — the scope of the Comptroller General's access-to-records authority.

2. *Amici* Contend that No Cost Records are Directly Pertinent to the Types of Contracts Involved in these Related Cases.

The position advanced by respondent Bristol in this case, however, is narrower than that presented by Merck and SmithKline in their parallel challenges to the Comptroller General's access demands. Bristol agreed to make available the records of production costs allocated to the specific products purchased under the particular contracts listed in the demand letter. In contrast, Merck and SmithKline have declined to make any cost records available to the Comptroller General. The *amici* believe that, under the access statutes, neither internally allocated costs nor unallocated costs are "directly pertinent" to "the contract" whenever — as in these cases — the contract price was not negotiated on the basis of the contractor's costs and the contractor made no representations about the nature or extent of its costs. This brief places before the Court what *amici* consider to be the proper interpretation of the scope of the access-to-records statutes.

3. The Pending Cases Involving *Amici* Present an Additional Issue Regarding the Lawfulness of the Purpose for Which Access was Demanded.

Unlike Bristol, which focused solely on the excessive scope of the access demands, the *amici* have also contended that the

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(footnote continued)

Staats, 483 F. Supp. 712 (E.D. Pa. 1980), *appeal pending*, 3d Cir. No. 80-1464 (filed Mar. 19, 1980), *conditional petition for certiorari before judgment denied*, No. 80-434 (Dec. 8, 1980).

A fourth company also brought suit challenging an identical access-to-records demand, *Eli Lilly & Co.* v. *Staats*, 574 F.2d 904 (7th Cir.), *cert. denied*, 439 U.S. 959 (1978); and the Government brought suit against a fifth, *United States* v. *Abbott Laboratories*, 597 F.2d 672 (7th Cir. 1979).

Comptroller General exceeded his statutory authority by making these demands for an improper purpose. Rather than using the access authority to audit individual government contracts as Congress intended, the Comptroller General served the demands on Bristol and the *amici* to secure cost data on individual pharmaceutical products sought by two Senators and their staffs and to gather data for an economic study by GAO of the pharmaceutical industry. *See* pp.25-26, *infra*.[6] This issue of GAO's improper purpose, which is not presented by this case, should be reserved by this Court for determination by the two Circuits before which the issue is now pending.[7]

SUMMARY OF THE ARGUMENT

The issue raised by this case is the scope of the Comptroller General's right of access under 10 U.S.C. § 2313(b) and 41 U.S.C. § 254(c) to the records of the thousands of corporations that contract with agencies of the federal government for the supply of an infinite variety of goods and services.

1. The statutory language contains express words of limitation restricting the scope of the Comptroller General's access authority to records that "directly pertain to" and "involve transactions relating to" specific contracts. The contracts on which the GAO premised its access demands to Bristol

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[6] Several commentators have concluded that the access demands served on Bristol, the *amici*, and three other pharmaceutical companies should be unenforceable because they were made for the unauthorized purpose just described. *See* Note, *Eli Lilly & Co. v. Staats: An Undue Expansion of the GAO's Investigatory Power Under the Access-to-Records Statutes*, 74 Nw. L. Rev. 122, 127-30 (1979); Comment, *The Comptroller General's Authority to Examine the Private Business Records of Government Contractors: Eli Lilly & Co. v. Staats*, 92 Harv. L. Rev. 1148, 1152, 1156 (1979).

[7] Merck and SmithKline filed conditional petitions for certiorari before judgment in their respective cases in order to afford this Court the opportunity to address all issues raised by these related cases at one time. In opposing these petitions, the government argued that the improper purpose question presents a distinct issue that should be considered first by the courts of appeals so that "this Court would have the benefit of full explication" of their views before determining whether to examine this question. *See* Brief for Respondents in Opposition in *SmithKline Corporation* v. *Staats*, No. 80-434 at 18.

and the *amici* were fixed-price contracts whose prices were not negotiated on the basis of costs but instead were based exclusively on the contractor's established catalog prices or other evidence of adequate price competition. Application of the statutory words of limitation to this category of contracts demonstrates that no cost records come within the scope of the access-to-records provision. The sweeping interpretation of the statutes proffered by the government, which would require that contractors open virtually all of their business records to government inspection, must be rejected as incompatible with the critical limiting language of the statutes.

2. The limited scope of the authority granted to the Comptroller General by Congress is underscored by the legislative history of the access-to-records statutes. Those statutes had their origin in emergency legislation adopted during the Korean War and were adopted solely to deter "fraud," or "overreaching" or "improprieties" in the negotiation of government contracts. The access authority was intended to accomplish this purpose by "enabl[ing] the Comptroller General to make effective audits" of individual contracts through examination of both the government records and the contractors' books. When, as in the present case, no cost data are submitted during the negotiation process and when the payments to the contractor do not depend on its cost of performance, the contractor's cost records are not "directly pertinent to" the limited audit contemplated by Congress.

3. The restricted scope of GAO's access authority evident from the statutory language employed by Congress and from the legislative history forecloses reliance on any contrary administrative interpretation of the statutes. Even if consideration of GAO interpretations were appropriate, however, this inquiry would not assist the government. GAO's current interpretation of the access-to-records statutes conflicts with GAO's contemporaneous construction of the proposed statute presented to Congress during its consideration of the bill. The new, expansive gloss asserted here also conflicts with GAO's repeated acknowledgements of the limits of its access authority.

4. Contrary to the government's assertion, rejection of its sweeping interpretation of the access statutes would neither

"render meaningless the Comptroller General's right of access" nor "totally defeat his statutory responsibility." Pet. Br. 15. In the past the Comptroller General has used his access authority exclusively to audit cost-based contracts in order to determine the accuracy of cost and pricing data supplied to government procurement officers during the negotation of the contracts. Neither the position advanced by Bristol on the scope of the Comptroller General's access authority nor that asserted by the *amici* presents the slightest threat to GAO's continued performance of its contract audit responsibilities. *Amici* submit only that a manufacturer's cost records are not "directly pertinent" to competitively priced contracts that were not negotiated on the basis of costs.

ARGUMENT

I. UNDER THE PLAIN MEANING OF THE ACCESS-TO-RECORDS STATUTES, NO COST INFORMATION IS "DIRECTLY PERTINENT" TO FIXED-PRICE CONTRACTS THAT WERE NOT NEGOTIATED ON THE BASIS OF COSTS.

As this Court has counseled, "'[t]he starting point in every case involving construction of a statute is the language itself.'" *Southeastern Community College* v. *Davis*, 442 U.S. 397, 405 (1979), *quoting Blue Chip Stamps* v. *Manor Drug Stores*, 421 U.S. 723, 756 (1975)(Powell, J., concurring). Here, the statutes on which the access-to-records demands are based — 10 U.S.C. § 2313(b) and 41 U.S.C. § 254(c) — grant the Comptroller General access only to books and records of the contractor that "directly pertain to," and "involve transactions relating to," the specific "contract."[8] As the District Court found, and the Second Circuit confirmed, these critical phrases are words of limitation that restrict the scope of the access authority granted by Congress. Pet. App. 3a, 10a.

Application of these words of limitation to the specific types of contracts involved in this case and in the related cases involving the *amici* demonstrates that no cost records of these

[8] The statutes are reprinted in Appendix A, *infra*, pp. 2a-3a.

contractors come within the scope of the access provision. As the government has acknowledged, all of the contracts involved in these cases are fixed-price rather than cost-based contracts. *See* Pet. Br. 3. In each instance, there was no actual negotiation of prices; no cost or pricing data were requested by the government purchasing agency in connection with the award of the contract; and the contractor made no representations about its costs in quoting its price for each product.[9] Instead, unlike many "negotiated" government contracts, the contract prices here were established on the basis of the contractors' published catalog prices at which these standard commercial items were sold to the public, or on the basis of other evidence of adequate price competition in the public marketplace. Under the federal procurement statutes, it was unnecessary to submit cost or pricing information in connection with the award of these contracts since competitive market forces established the reasonableness of the contract prices.[10] In these circumstances, the contractors' cost records do not "directly pertain to" or "involve transactions relating to" these contracts.

The Ninth Circuit's decision in *Hewlett-Packard Co.* v. *United States,* 385 F.2d 1013, 1016 (9th Cir. 1967), *cert. denied,* 390 U.S. 988 (1968), recognized that if "costs were not taken into consideration in arriving at the terms and conditions of the contracts in question," and if the proper focus is the specific terms and conditions of the contract that gives rise to the access demand, then records relating to costs "could not be said to directly pertain to, and involve transactions relating to, the contract, as so defined." This is the position that *amici* advance here.

The Ninth Circuit went astray, however, by adopting a strained and unnatural definition of the term "contract." *See*

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[9] Merck C.A. App. 140-45; SmithKline C.A. App. 75-76, 342.

[10] Under the Truth-in-Negotiations Act, 10 U.S.C. § 2306(f), contractors are normally required to submit cost and pricing data to the government as part of the negotiation process. Congress, however, expressly exempted from this requirement the types of contracts involved in these cases — contracts "where the price negotiated is based on adequate price competition" or on "established catalog or market prices of commercial items sold in substantial quantities to the general public."

385 F.2d at 1016. The court inexplicably interpreted "contract" as "embracing not only the specific terms and conditions of the agreement, but also the general subject matter" — "the procurement of described property by the goverment." *Id.* This error expanded the category of information the court considered "directly pertinent to" the "contract."[11]

A fundamental canon of statutory construction is that, "unless otherwise defined, words will be interpreted as taking their ordinary, contemporary, common meaning." *Perrin* v. *United States,* 444 U.S. 37, 42 (1979); *Burns* v. *Alcala,* 420 U.S. 575, 580-81 (1975). The term "contract" has traditionally and commonly been understood to refer to a specific agreement between two parties. *See, e.g., Fletcher* v. *Peck,* 10 U.S. (6 Cranch) 87, 136 (1810); *Larson Construction Co.* v. *Oregon Auto Ins. Co.,* 450 F.2d 1193, 1195 (9th Cir. 1971). Significantly, this same, commonplace definition of contract was contained in federal procurement regulations in force at the time Congress enacted the access-to-records statute in 1951, 32 C.F.R. § 400.201(6) (1951), and it continues to be used in the regulations in force today, 41 C.F.R. § 1-1.208 (1979).[12]

This "ordinary meaning" of "contract" is reinforced here by the manner in which the term "contract" is used elsewhere in the same section of the statute. The mechanism employed by Congress in creating the access-to-records authority was to require the inclusion of an access clause in all "*contracts* negotiated without advertising." Act of October 31, 1951, Pub. L. No. 82-245, 65 Stat. 700 (emphasis added). There can be no doubt that the word "contract" was employed in that phrase to mean a specific, formal agreement between two parties, since

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[11] Nothing in the access provisions themselves or their legislative history justifies this novel interpretation, which has been sharply criticized *See, e.g., Eli Lilly & Co.* v. *Staats, supra,* 574 F.2d at 918-19 (Pell J., dissenting); Note, *Eli Lilly & Co. v. Staats: An Undue Expansion of the GAO's Investigatory Power Under the Access-to-Records Statutes,* 74 Nw. L. Rev. 122, 130-31 (1979); *cf. United States* v. *Abbott Laboratories, supra,* 597 F.2d at 674-75.

[12] 32 C.F.R. § 400.201(6) (1951) provided:

"The term 'contracts' means all types of agreements and orders for the procurement of supplies or services."

only such agreements contain "clauses" and are subject to negotiation. Since it "is hardly credible that Congress used the term [contract] in different senses in the same sentence," *United States* v. *Cooper Corp.*, 312 U.S. 600, 606 (1941), it is clear that "contract" as used in the access-to-records statute refers to the specific agreement between two parties.[13]

Given this "ordinary meaning" of the term "contract," it is easy to apply the statutory restriction that only those records that "directly pertain" to the specific contract may be examined. When the contractor has made no representations to the government purchasing agency about its costs but instead has offered the product at a fixed price equal to or below the price established in the competitive commercial market, the Comptroller General's limited access right does not extend to records reflecting the manufacturer's costs or its pricing methodology.

The government's sweeping interpretation of GAO's access-to-records authority completely ignores the express limiting language of the statute. According to the government, "all costs met in whole or in part from revenues earned" on a particular government contract are within the scope of the access-to-records provision. Pet. Br. 7, *quoting* Pet. App. 9a. The overreaching inherent in this claim is magnified when all revenues are commingled in a general corporate account and are used as required to meet all of a company's ongoing expenses. This is the accounting practice followed by Bristol and the *amici*, and almost certainly by most other government contractors. In this situation, the government's theory encompasses records of all costs "defrayed by the contractor from commingled general revenues that include the government's payments under the contracts." Pet. Br. I.

This interpretation produces absurd results, since the matching of revenues from a particular contract with a manu-

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[13] The legislative history of the access-to-records statute lends further support to this analysis of the meaning of "contract." For example, the sponsor of the access-to-records provision emphasized that the "right [of access] is given [the Comptroller General] in the contract. The right is not given him in the bill." 97 Cong. Rec. 13376 (1951) (remarks of Rep. Hardy); *see id.* at 13198 (remarks of Rep. Hardy).

facturer's range of costs may well be completely arbitrary. For example, a payment received as a result of a given government contract may be used to purchase raw materials for use in manufacturing an entirely different product than that purchased under the contract. The revenue from a sale to the government may become part of an investment in the stock of another corporation, or it may go to pay the salaries of scientists performing research on potential products that may not be marketed for ten years—if ever.

In virtually all cases, the revenues earned on a particular contract will be received after performance. Therefore, they will not relate to the period in which the costs of performing that contract were incurred. This is particularly true for research and development costs in the pharmaceutical industry which of necessity are incurred *many years* before the product is first sold to anyone.[14] The government's construction of the statute thus would permit examination of cost records that not only are unrelated to the contract on which the access demand is premised but also have nothing at all to do even with the product that was procured through the contract.

The District Court found, against this backdrop, that the government's theory is virtually limitless in its sweep, potentially reaching all of the contractor's records relating to all costs of all products. Pet. App. 9a. Since the revenues generated by even the smallest government contract would, as part of the contractor's commingled general revenues, theoretically contribute "in part" to the recovery of all costs, a *single* negotiated government procurement contract would permit the Comptroller General to demand access to all of the contractor's business records.[15] The courts below, therefore, properly rejected the government's interpretation of the access-to-records statutes.

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[14] It now takes, on average, 7 to 10 years to complete the elaborate testing process required by the FDA before a new drug can be marketed. 127 Cong. Rec. S674 (daily ed., Jan. 27, 1981)(remarks of Sen. Mathias).

[15] A senior GAO official acknowledged this consequence of the government's interpretation of the access-to-records provision during a deposition taken in the *Merck* case. *See* Merck C.A. App. 338 (Deposition of Gregory J. Ahart, Director, Human Resources Division, General Accounting Office) (reprinted in Appendix B, *infra*, pp. 5a-6a).

The government's position is in square conflict with Congress' decision to limit the Comptroller General's access only to "directly pertinent" records. *See* Pet. App. 10a. No cost records fall within this limited compass where contract prices are neither cost-based nor negotiated on the basis of costs.

II. THE LEGISLATIVE HISTORY OF THE ACCESS-TO-RECORDS STATUTES UNDERSCORES THE LIMITED AUTHORITY GRANTED THE COMPTROLLER GENERAL.

The legislative history makes clear that the access-to-records provision was enacted for the limited purpose of deterring or detecting abuses in the negotiation process by facilitating GAO audits of individual procurement contracts. In performing the contract audits contemplated by Congress, GAO has no need for access to cost records of government contractors — such as those of the *amici* here — that were not put forward as support for the price and were not used as a basis for computing the payment made by the government. Since these records are not relevant to the detection of misrepresentations in the negotiation of the contract price or of overcharges in the request for payment, they are not "directly pertinent" to the "transactions involving" the contract.

A. The Limited Purpose Of The Access-To-Records Statutes Is Evident From Their Origin In Emergency Legislation.

The access-to-records clauses involved in this case were required by an October 1951 statute. Pub. L. 82-245, 65 Stat. 700.[16] That statute was modeled on, and as originally proposed was identical to, an amendment to the First War Powers Act that had been adopted by Congress in January 1951. Act of January 12, 1951, 64 Stat. 1257. The legislative history of that predecessor statute is critical to a proper understanding of the

[16] The October 1951 statute amended both section 4 of the Armed Services Procurement Act of 1947, 10 U.S.C. § 2313(b), and section 304 of the Federal Property and Administrative Services Act of 1949, 41 U.S.C. § 254 (c), to require the inclusion of access-to-records clauses in virtually all negotiated government procurement contracts. The October 1951 statute is reprinted in Appendix A, *infra*, p. 2a.

Comptroller General's access-to-records authority. *See, e.g., Oscar Mayer & Co.* v. *Evans,* 441 U.S. 750, 755-56, 758 (1979); *Cannon* v. *University of Chicago,* 441 U.S. 677, 694-98 (1979).

The January 1951 amendment to the First War Powers Act was adopted in response to crisis conditions created by the Korean War. Rampant inflation and skyrocketing costs fueled by the war made it difficult for many defense contractors operating under fixed-price contracts to keep their commitments to supply the government with vital munitions. *See* H.R. Rep. No. 3227, 81st Cong., 2d Sess. 3-4 (1950); S. Rep. No. 2686, 81st Cong., 2d Sess. 2 (1950). In response, Congress reinstated the emergency authority created during World War II to negotiate increases in contract prices, but only for an 18-month period. *See* S. Rep. No. 2686, *supra,* at 3; Act of January 12, 1951, § 2, 64 Stat. 1258.

To allay concern about possible abuse of the authority to increase contract prices, *e.g.,* 96 Cong. Rec. 17045 (1951) (remarks of Rep. Marcantonio), Representative Hardy offered an amendment to the bill to provide the Comptroller General with authority to examine "pertinent" records relating to any contracts renegotiated under the statute. *Id.* (Remarks of Rep. Hardy). The bill's floor manager explained that the access-to-records amendment was proposed for the limited purpose of deterring and detecting abuse of the emergency negotiating authority:

> "The amendment will give power to the General Accounting Office to go into the books and delve into the records of these contractors who have been relieved *to determine whether or not there is fraud or overreaching or whether they have done anything untoward,* in which event reports will be made and suitable action may be taken. The power of investigation and inquiry of the General Accounting Office should be an excellent deterrent. These reports also would

be of great help subsequently on the question of renegotiation." *Id.* at 17123 (remarks of Rep. Celler)(emphasis added).[17]

B. The Permanent Access-To-Records Statutes Were Enacted For the Same Limited Purpose.

Shortly after the adoption of the First War Powers Act amendments, Representative Hardy learned that government procurement officers were also negotiating wartime contracts under two permanent procurement statutes — the Armed Services Procurement Act of 1947 and the Federal Property and Administrative Services Act of 1949. *See* 97 Cong. Rec. 13198 (1951). Those statutes lacked any access-to-records provisions. *Id.* "In order to plug this loophole," Representative Hardy introduced a bill to require the inclusion of access-to-records clauses in contracts negotiated under these statutes. *Id.* Both the House and Senate reports echo his explanation that the bill was intended "merely" to "carr[y] into our general procurement statutes the same principle" embodied in the First War Powers Act amendments. *Id.* (remarks of Rep. Hardy); *see id.* at 13199, 13200; H.R. Rep. No. 791, 82d Cong., 1st Sess. 2 (1951); S. Rep. No. 603, 82d Cong., 1st Sess. 2 (1951).

Representative Hardy explained that his "main purpose in offering this bill was to place on the statute books a law which will act as a deterrent to improprieties in the negotiation of Government contracts." 97 Cong. Rec. 13198 (1951). The access-to-records provision was intended to provide such a deterrent by "enabl[ing] the Comptroller General to make effective audits" of the accounts of government contracting officers. *Id.* at 12611 (1951). As he explained:

"[T]he audit which GAO performs is directed primarily to the accounts of the accountable officers of the Government

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[17] This power to detect overcharges reinforced the government's right under the Renegotiation Act of 1951 to recoup payments made for unwarranted costs billed to the government. The government has acknowledged, however, that the Renegotiation Act did not apply to the contracts of Bristol and the *amici* because Congress has exempted contracts for standard commercial items whose prices are set in the competitive market place. 50 U.S.C. App. §§ 1216(e)(1)(A) & (4)(B). *See* Merck C.A. App. 143.

and not to the contractors themselves. The GAO is required by law to take exceptions against accountable officers for erroneous or illegal payments." *Id.* at 13197.[18]

The access-to-records authority was to assist in deterring and detecting erroneous or illegal payments to contractors by enabling the Comptroller General "to check the transaction, both from the Government records and the contractors' books." *Id.* at 13198 (remarks of Rep. Hardy). The access authority thus would serve to safeguard against neglect of responsibilities by government personnel and against such contractor abuses as the inflating of overhead rates quoted to procurement officers during contract negotiations and the improper shifting of costs from fixed-price contracts to cost-plus contracts. *Id.* [19] Where,

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[18] The access authority was intended to focus on auditing the contracting officer's handling of individual contracts. At the time the statute was adopted, GAO's primary function was the settlement of the accounts of government disbursing officers:

> "The central and best known of the GAO's responsibilities was the *audit of expenditure vouchers* (mostly after they had been paid) and the *settlement of accounts* — primarily those of the various disbursing officers scattered around the government — which were required to be submitted periodically along with all their supporting documents. The GAO's checking of individual vouchers was intended to assure that the money was authorized and available, the payment was lawful in every respect, the proper procedures had been followed, *and no fraud or other irregularity was involved.* If any objections were raised, notices of exception were issued to the responsible officers, and unless satisfactory explanation could be made the payments were disallowed." F. Mosher, *The GAO: The Quest for Accountability in American Government* 72-73 (1979) (footnote omitted; first emphasis in the original; second emphasis added).

Commentators writing in the early 1950's, shortly after the access-to-records statute was adopted, noted that the access authority was designed to enable GAO to discharge these audit and settlement responsibilities. *See, e.g.*, Cable, *The General Accounting Office and Finality of Decisions of Government Contracting Officers*, 27 N.Y.U.L. Rev. 780, 782 (1952); Welch, *The General Accounting Office in Government Procurement*, 14 Fed. B. J. 321, 326 (1954).

[19] The examples set forth in the legislative history deal with situations in which inaccurate cost information is supplied by the contractor to the procurement officer in order to obtain a higher negotiated price or an inflated

(footnote continues)

as in the present case, the contractor's cost records did not enter into the negotiation of the contract and were never considered by the government procurement officer in awarding the contract or authorizing payments to the contractor, there is no reason to examine those records in auditing the transaction.

The statements focusing on the statute's limited audit purpose are reinforced by the explanations for two important amendments adopted on the House floor circumscribing the access-to-records authority. Even as originally introduced, the bill was to limit the Comptroller General to "pertinent" records of the contractor "involving transactions related to" the specific procurement contract. During the House debates this language was tightened further to restrict the Comptroller General to records that are "directly" pertinent to the contract. Representative Hoffman, who sponsored the amendment, stated that it was intended "to limit the 'snooping' that may be carried on under the bill." 97 Cong. Rec. 13377 (1951).

The other amendment limited to three years from the date of final payment under the contract the time period during which the Comptroller General may demand access to a contractor's records. In adopting this limitation, Congress demonstrated that it viewed the access-to-records authority as a limited adjunct to GAO's power to audit the accounts of government disbursement officers and disallow erroneous payments, a power also restricted to a three-year period. *Id.* at 13199 (remarks of Rep. Hardy).

These amendments confirm the limited purpose of the access rights to audit the conduct of contract negotiation and the documentation for payment. When cost and pricing records are submitted as part of the negotiation process or in connection with a claim for payment under a cost-reimbursement type of contract, those records are "directly pertinent" to the contract. Through examination of such records, GAO can detect fraud or

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(footnote continued)

payment on cost-based contracts. *See* 97 Cong. Rec. 13198 (1951). One example refers to the setting of the "overhead rate," a cost item, in construction contracts. The government in its brief distorts the legislative history by repeatedly substituting the word "price" where the word "rate" appears in the debates. *See* Pet. Br. at 9, 16, 17.

overreaching by contractors who inflate their cost estimates or who seek payment for costs acutally incurred in connection with other contracts or for which reimbursement has already been obtained. This examination enables GAO to discover illegal or erroneous payments by government contracting officers. By contrast, when no cost data are submitted during the negotiating process, and when contract payments do not depend on the contractor's costs of performance, the contractor's cost and pricing records are irrelevant to the type of GAO audit contemplated by Congress. There can be no fraud or overreaching in the negotiation process where, as here, the contract is awarded on the basis of the contractor's established commercial catalog price for the item. The only records that are pertinent to an audit of fixed-price contracts where costs have never been a subject of the negotiation process are those required to show that the contractor actually had an established catalog price for the item procured and to verify that the sum received in payment from the government was the amount due under the contract.[20]

C. The Government's Interpretation Of The Statutes Conflicts With Their Legislative History.

The government argues that this Court should ignore the express limiting language of the statutes because the legislative history allegedly "makes clear that Congress intended the Comptroller General to have a broad right of access" to evaluate the reasonableness of contract prices and to study the adequacy of government negotiating techniques. *See* Pet. Br. 15, 34. As one commentator has noted, however, and as even the government's brief reveals, there is nothing in the legislative history indicating that the access-to-records authority was designed to enable GAO to evaluate the abstract "reasonableness" of a price and, through that device, to assess the adequacy of government procurement procedures. *See* Note,

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[20] Merck has offered to make such records available so that GAO can confirm that their contracts were properly negotiated on the basis of the catalog price exemption to the Truth-in-Negotiations Act, 10 U.S.C. § 2306(f), and can verify that there were no overpayments by contracting officers. Merck C.A. App. 100-01. SmithKline would be willing to make the same showing.

Government Contracts: Contractor's Obligation to Allow Examination of Records Under 10 U.S.C. 2313(b), 72 Dick. L. Rev. 687, 691 (1968). The absence of any reference to such an "assessment function" strongly suggests that Congress' "purpose was solely to provide a method to discover fraudulent activities and not a means by which government agencies can improve their procurement techniques for use in future contracts." *Id.*

The only "support" offered by the government for the purpose it ascribes to the statute consists of a few carefully edited phrases taken from the House debates and several statements of concern from opponents of the statute. *See* Pet. Br. 15-18. For example, in a misleading effort to create the impression that evaluation of the abstract fairness of contract prices was a concern of Congress, the government on four occasions simply inserts the word "price" into quotations from the legistative history. *See* Pet. Br. 9, 16, 17. As they appear in the Congressional Record, however, the passages excerpted and altered by the government deal only with misrepresentations of *costs* during negotiations. *See* n. 19, *supra.*

Similarly, the government repeatedly refers to the Comptroller General's broad statutory powers to investigate and make reports concerning the expenditures of the executive branch, implying that Congress intended the grant of access authority to be used as an open-ended research "tool" by the Comptroller General. *See* Pet. Br. 8-9, 13, 16-17. Read in context, however, the passage quoted by the government (Pet. Br. 9) refers only to giving GAO the "proper tools" to audit accounts of government contracting officers. No member of Congress ever suggested that the limited access right could be used in connection with the Comptroller General's other, unrelated functions, as now suggested by the government's cropped quotation. In fact, none of the other statutes relied on in the government's brief, 31 U.S.C. §§ 53(a), 60 and 65(a), was even mentioned in the legislative history.[21]

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[21] Those provisions do no more than establish GAO's authority to evaluate the activities of governmental agencies through "management"

(footnote continues)

The statements from opponents of the bill quoted by the government provide no support for its interpretation of the statute. *See* Pet. Br. 17-18. As this Court has repeatedly counseled, statements by opponents "have scant probative value" because, in "their zeal to defeat a bill, they understandably tend to overstate its reach." *National Woodwork Manufacturers Ass'n* v. NLRB, 386 U.S. 612, 639-40 (1967), *quoting, NLRB* v. *Fruit & Vegetable Packers,* 377 U.S. 58, 66 (1964); *accord, Schwegmann Brothers* v. *Calvert Distillers Corp.,* 341 U.S. 384, 395 (1951) ("The fears and doubts of the opposition are no authoritative guide to the construction of legislation."). Moreover, Congress responded to the objections of overbreadth by deliberately confining the access right only to "directly" pertinent records.[22]

The government's interpretation of the access-to-records statute is simply incompatible with (i) its origin in temporary emergency legislation that created a risk of fraud and overreaching, (ii) the deliberate addition of language that narrowed the scope of access, and (iii) the limitation of the access right to the period during which GAO may audit government accounts. These legislative choices would make no sense if Congress had intended to authorize GAO to use the access right to assess and refine negotiating techniques for future government procurement efforts.

III. GAO'S CURRENT INTERPRETATION OF THE ACCESS-TO-RECORDS STATUTES IS NOT ENTITLED TO JUDICIAL DEFERENCE.

The government also argues that the Second Circuit erred in failing to accord substantial deference to what it asserts is

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(footnote continued)

reviews and oversights. They contain no authorization of any kind for the examination of otherwise private records of government contractors. *See* Cibinic and Laskin, *The Comptroller General and Government Contracts,* 38 Geo. Wash. L. Rev. 349, 387-88 (1970).

[22] It was after those expressions of concern that Representative Hoffman (one of the opponents) offered his amendment to restrict the Comptroller General to *directly* pertinent records in order to prevent "snooping" by GAO. *See* p. 16, *supra.*

GAO's "consistent and longstanding construction" of the access-to-records statute. Pet. Br. 22-30. Even if the sweeping position asserted in this dispute were part of a consistent and longstanding interpretation of the statute, it should not prevail, since it conflicts with "the clear meaning of a statute, as revealed by its language, purpose and history." *Southeastern Community College* v. *Davis,* 442 U.S. 397, 411 (1979), *quoting Teamsters* v. *Daniel,* 439 U.S. 551, 566 n.20 (1979). Here, the Court has a "clear duty . . . to reject the administrative interpretation of the statute." *SEC* v. *Sloan,* 436 U.S. 103, 119 (1978).

Moreover, the Court should "accord no special weight" to GAO's current interpretation, because it is actually at odds with the Agency's contemporaneous construction of the statute and with GAO's repeated acknowledgements of the limits of its access authority. *United Housing Foundation, Inc.* v. *Forman,* 421 U.S. 837, 858-59 n.25 (1975). Far from acquiescing in GAO's current view of its access authority, as the government asserts, Congress has acted to guard against the kind of sweeping access demands made by the Comptroller General in this case.

A. GAO's Contemporaneous Construction Of The Statutes Conflicts With Its Position Here.

As this Court has explained, an administrative construction of a statute " 'carries most weight' " when adopted in connection with Congress' consideration of the legislation and when " 'directly made known . . . to Congress in committee hearings.' " *SEC* v. *Sloan, supra,* 436 U.S. at 120, *quoting Zuber* v. *Allen,* 396 U.S. 168, 192 (1969).

Here GAO's contemporaneous interpretation emphasizing the limited purpose and scope of the access-to-records statute was presented to Congress by the Acting Comptroller General during Congress' consideration of the bill. *See* H.R. Rep. No. 791, *supra,* at 4-5; S. Rep. No. 603, *supra,* at 3-4. The GAO's official explanations of the proposal clearly express the agency's

understanding that the access-to-records provision was intended *solely* as a deterrent to improprieties in contact negotiations.[23] The government, inexcusably, fails to mention GAO's contemporaneous construction of the access-to-records provision, which flatly contradicts its current interpretation.

B. GAO Has Repeatedly Acknowledged The Limited Scope Of Its Access-To-Records Authority.

Not only does GAO's contemporaneous construction of the access-to-records statute conflict with its position here, but other intervening GAO statements also are inconsistent with the sweeping access demands made to Bristol and the *amici.*

For example, although GAO now claims that it may examine records relating to the commercial business of Bristol and the *amici* in order to assess the adequacy of government negotiating techniques and the fairness of prices charged the government, GAO has repeatedly stated that it has no authority to demand access to such records. In the 1965 hearings cited by the government (Pet. Br. 26-27), GAO's general counsel testified that GAO had no right to examine records pertaining

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[23] In similar letters to the House and Senate committee chairmen, GAO stated that the "purpose and intended effect of such legislation is clearly explained" in a passage quoted from the House floor debates on the First War Powers Act amendments:

> "Mr. Celler. As I understand the Hardy amendment, the powers given are like a Damoclean sword that will hang over the heads of the contractors whose contracts are changed. The amendment will give power to the General Accounting Office to go into the books and delve into the records of these contractors who have been relieved *to determine whether or not there is fraud or overreaching or whether they have done anything untoward,* in which event reports will be made and suitable action may be taken. The power of investigation and inquiry of the General Accounting Office should be an excellent deterrent." H.R. Rep. No. 791, *supra,* at 4 (emphasis added).

The letters concluded:

> "It is apparent that the proposed legislation herein considered likewise *is intended as a deterrent to those persons who otherwise might abuse the authority* to negotiate certain contracts without advertising." *Id.* (emphasis added).

to "any commercial business" of the contractor.[24] In 1967, the Acting Comptroller General emphasized this important limitation in ruling that GAO personnel could not insist upon examining records relating to a contractor's commercial business, even where review of such records would be necessary to determine whether a catalog-priced item was actually sold in substantial quantities to the general public, as the contractor had represented. GAO Opinion B-162009-O.M. (August 31, 1967) (reprinted in Appendix C. *infra,* pp. 8a-9a). This limitation on records related to a contractor's commercial business has been repeated in other opinions and in testimony to Congress by Comptroller General Staats. *See, e.g.,* GAO Opinion B-141683-O.M. (June 5, 1968) (App. C, *infra,* pp.10a-11a); *Hearings on the Military Budget and National Economic Priorities Before the Subcomm. on Economy in Government of the Joint Economic Comm.,* 91st Cong., 1st Sess. 714 (1969).

GAO also emphasized the limited scope of its access-to-records authority in the late 1960s and early 1970s when it sought expanded authority from Congress in order to perform "should cost" reviews of government contractors. Internal GAO memoranda, which were obtained through discovery in the companion cases in which the *amici* are parties, and which are part of the records in those cases, reveal that in 1970 GAO believed it needed additional authorization from Congress in order to examine a variety of records, including those involving a contractor's "indirect costs" — the very type of records at issue in this case. *See* GAO Memorandum B-159896(.07) (October 22, 1970)(App. C, *infra,* pp.12a-13a). In connection with its request for legislation expanding its access authority, GAO provided Congress with a memorandum emphasizing the limited nature of its access-to-records authority. *See* 115 Cong. Rec. 25800-01 (1969). This memorandum noted that GAO does not have authority to examine a contractor's capital investment data or to attempt to allocate the contractor's capital investment between its defense and non-defense work. 115

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[24] *Hearings on Comptroller General Reports to Congress on Audits of Defense Contracts Before a Subcommittee of the House Committee on Government Operations,* 89th Cong., 1st Sess. 165 (1965) (testimony of Robert Keller).

Cong. Rec. 25800 (1969); *see Hearings on the Military Budget and National Economic Priorities, supra,* 714 (testimony of Comptroller General Staats).

In sum, this litigation is the first occasion on which GAO has asserted the kind of unlimited access authority that it now seeks to uphold.

C. Subsequent Congressional Actions Reveal A Continuing Intention To Circumscribe GAO's Access Authority.

The government asserts that Congress has approved GAO's interpretation of the access-to-records statute by its silence. Pet. Br. 29-30. As this Court has repeatedly counseled, however, "legislative silence is a poor beacon to follow in discerning the proper statutory route." *Zuber* v. *Allen,* 396 U.S. 168, 185 (1969); *see, e.g., Girouard* v. *United States,* 328 U.S. 61, 69 (1946). Here, as shown above, the prerequisite to such an acquiescence argument — a consistent, long-standing administrative construction that has been repeatedly presented to Congress and carefully considered by it — is plainly absent. *Compare SEC* v. *Sloan, supra,* 436 U.S. at 121 ("We are extremely hesitant to presume general congressional awareness of the Commission's construction based only upon a few isolated statements in the thousands of pages of legislative documents") *with* Pet. Br. 24-28.[25]

Actions taken by Congress since the passage of the access-to-records statute in 1951 belie GAO's claim that Congress has acquiesced in an assertion of sweeping authority. On only one

[25] An exchange in the 1965 hearings cited by the government reveals that there was not even passive acceptance of the isolated GAO statements relied upon by the government. *See Hearings on Comptroller General Reports to Congress on Audits of Defense Contracts, supra,* at 649-53. During these hearings, the committee counsel pressed Comptroller General Weitzel to reconcile his view of GAO's access authority with the legislative history of the statute, which demonstrates that the access right, like that granted by the January 1951 amendment to the First War Powers Act, was merely designed to deter "fraud and overreaching." *Id.* at 649-53. The Comptroller General's contention that the October 1951 statute had a "broadened" purpose, *id.* at 652, was disputed by the skeptical committee counsel, *id.* at 653.

occasion has Congress deliberately granted GAO the broad-ranging authority that it has attempted to assert here. As part of the Military Appropriations Act of 1970, Congress authorized GAO to engage in a study of defense industry profits. *See* Pub. L. No. 91-121, § 408, 83 Stat. 208. Significantly, this authority was conferred only for one year, and it was limited to "only a single study." 115 Cong. Rec. 25793 (1969) (remarks of Senator Proxmire); *id.* at 25795 (remarks of Senator Ribicoff). In 1973, and again in 1975, Congress turned a deaf ear to several GAO-drafted proposals that would have authorized GAO to demand broad-based access to contractors' records in order to conduct profit studies of companies having government contracts aggregating more than $1,000,000 during the most recent fiscal year.[26] Since Congress withheld this power when GAO expressly sought it with respect to such large contractors, it is absurd to argue that even broader power regarding all contractors has already been implicitly inserted in the 1951 legislation through Congressional silence.

IV. REJECTION OF GAO'S SWEEPING INTERPRETATION OF THE ACCESS-TO-RECORDS STATUTES WILL NOT IMPEDE ITS ABILITY TO DISCHARGE ITS RESPONSIBILITIES.

The government's *in terrorem* assertion that "the decision below would render meaningless the Comptroller General's right of access and would totally defeat his statutory responsibility" (Pet. Br. 15) is belied by the record in this case and in the companion cases in which the *amici* are parties.

In order to demonstrate the importance of the access-to-records statute, the government submitted an affidavit by GAO's general counsel explaining that in fiscal years 1974 and 1975 GAO's Procurement and Systems Acquisition Division used the access authority to examine contracts and subcontracts totaling $814,900,000, and recovered more than $5,000,000 as a result of overpricing uncovered through its audits. *See* Merck C.A. App. 99-100 (¶ 4). The GAO's answers to interrogatories

[26] *See* S. 2049 and S. 3014, introduced during the 93d Congress, and S. 2268, introduced in the 94th Congress.

in the *Merck* case, however, admitted that *in every one* of those instances GAO was conducting individual audits of *cost-based* contracts in order to determine the accuracy of cost and pricing data supplied to government procurement officers during the negotiation of the contracts. Merck C.A. App. 147. Neither the Second Circuit's decision nor the contentions of Bristol and the *amici* present the slightest challenge to GAO's continued performance of contract audits or to its review of cost information pertinent to cost-based contracts.

Here, however, GAO does not even purport to be using its access authority to audit these particular *non*-cost-based contracts. Merck C.A. App. 146 (No. 8); Brief for the Respondents in Oppositon in *SmithKline Corp.* v. *Staats*, No. 80-434, at 7-8 n.6. Rather, the government has acknowledged that the access demands served on Bristol and the *amici* were issued to obtain data from pharmaceutical companies for use in a study of economic and operational aspects of the drug industry. J.A. 95 (¶ 6). The discovery taken in the *Merck* case revealed that GAO has *never before* attempted to use its access authority to gather data from contractors for such an industry study. Merck C.A. App. 246-81. This case, therefore, hardly presents a challenge to the ability of the GAO to conduct any well-established functions central to its duties.

The government's assertion that the Second Circuit's decision will interfere with GAO's ability to meet its responsibilities is also undermined by the fact that the GAO was pressured into making the access demands served on Bristol and the *amici*. The access demands were made as a result of pressure placed on GAO by two Senators who wanted to obtain raw cost data on individual drug products.[27] Before he acquiesed in persistent prodding to obtain drug company cost records, petitioner Staats had testified that securing such data would not serve any purpose useful to GAO, because "it would be impossible to develop from [the company's] internal accounts what their

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[27] *See SmithKline Corp.* v. *Staats*, *supra*, 483 F. Supp. at 716-17; *Eli Lilly & Co.* v. *Staats*, *supra*, 574 F.2d at 921-22; Note, *Eli Lilly & Co. v. Staats: An Undue Expansion of the GAO's Investigatory Power Under the Access-to-Records Statutes*, *supra*, 74 Nw. L. Rev. at 124.

costs are with respect to an individual drug." *Hearings on Competitive Problems in the Drug Industry Before the Subcomm. on Monopoly of the Senate Small Business Committee,* 92d Cong., 2d Sess. at 8753 (1972).

Petitioner Staats also had advised Congress that no "meaningful conclusions" could be developed on an individual product basis and that use of the access-to-records authority with respect to individual contracts would simply be "a waste of time." *Id.* at 8578. Indeed, rather than claiming a need to use the access-to-records statute "to evaluate the fairness of the contract price" (Pet. Br. 15), petitioner Staats testified that the government's interest in obtaining a fair price is protected by the market when, as here, the government purchases items at or below the catalog price at which the manufacturer sells the product to the public at large. *Id.* at 8580-81. These contemporaneous judgments about his real statutory interests deserve more credence than do the *post hoc* rationalizations of petitioner's lawyers.

CONCLUSION

The judgment of the Second Circuit should be affirmed on the basis of the statutory interpretation advanced above.

Respectfully submitted.

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APPENDIX A

Statutory Provisions

1. The October 31, 1951 Access-to-Records statute, 65 Stat. 700, provides:

> Section 304 of the Federal Property and Administrative Services Act of 1949 and section 4 of the Armed Services Procurement Act of 1947 are hereby amended by inserting at the end of the above-named sections the following new subsection:

"(c) All contracts negotiated without advertising pursuant to authority contained in this Act shall include a clause to the effect that the Comptroller General of the United States or any of his duly authorized representatives shall until the expiration of three years after final payment have access to and the right to examine any directly pertinent books, documents, papers, and records of the contractor or any of his subcontractors engaged in the performance of and involving transactions related to such contracts or subcontracts."

2. Section 4(c) of the Armed Services Procurement Act of 1947, 10 U.S.C. § 2313(b), provides:

> Except as provided in subsection (c), each contract negotiated under this chapter shall provide that the Comptroller General and his representatives are entitled, until the expiration of three years after final payment, to examine any books, documents, papers, or records of the contractor, or any of his subcontractors, that directly pertain to, and involve transactions relating to, the contract or subcontract.

3. Section 304(c) of the Federal Property and Administrative Services Act, 41 U.S.C. § 254(c), provides:

> All contracts negotiated without advertising pursuant to authority contained in this chapter, chapter 11C of Title 5, chapter 10 of Title 40, and chapter 11 of Title 44 shall include a clause to the effect that the Comptroller General of the United States or any of his duly authorized representatives shall until the expiration of three years after final payment have access to and the right to examine any

directly pertinent books, documents, papers, and records of the contractor or any of his subcontractors engaged in the performance of and involving transactions related to such contracts or subcontracts.

APPENDIX B

Ahart Deposition Testimony

Excerpts from the Deposition of Gregory J. Ahart, Director, Human Resources Division, General Accounting Office, taken in *Merck & Co., Inc.* v. *Staats,* No. 74-1447 (D.D.C.).

1. *Page 144 (Merck C.A. App. 338)*

Q. Well, we are back to "directly pertinent," again. How direct does "directly pertinent" have to be in order to come within your claim of right? Can you give me some feel for that?

A. Well, in answer to the Interrogatory that we are talking about here, one test is whether or not these affect the prices paid by the Government.

Q. Even though the company may not have taken them into account in establishing a price?

A. Even though the company may not have taken them specifically into account in establishing a price.

Q. The fact that they are there as a general ambient of the company's business is enough to make them directly pertinent to the performance of the contract?

A. In my judgment, that would be.

Q. And this is true even if a company only has one Government contract?

A. Since the access to records clause is brought to bear on an individual contract basis, yes.

2. *Pages 152-53 (Merck C.A. App. 346-47)*

Q. But you are unable, today, to give me any idea what the limitations on the time periods would be, is that correct?

A. Yes, that is correct. The constraints are as I stated but, without more specific knowledge than we possess, we can't be more specific.

Q. So even if costs were not considered in pricing a particular product, conceivably you would insist on the right to

records that might be 20 years old or might relate to costs incurred 20 years ago?

A. If they were determined to be directly pertinent to the contract.

Q. But we have no way of deciding how they might be directly pertinent. There is no way you can define how you would make that test.

A. If they affect the prices, if they are given consideration during the pricing of the—

Q. No, they are not given consideration by the company in making its pricing decision.

A. If they are not given specific consideration, we would have to make a judgment as to whether or not, irrespective of specific consideration, they affect the prices.

Q. In the sense that you described before, that they relate to the company's overall costs and, sooner or later, the company wants to make a profit on a company-wide or division-wide basis?

A. Yes.

APPENDIX C

GAO Opinions and Memoranda

B-162009-O.M. August 31, 1967

Director, Civil Division

Returned. The July 10, 1967, memorandum from Gregory J. Ahart, Deputy Director, Civil Division, requests advice regarding the right of General Accounting Office representatives to audit a Government contractor's sales records to ascertain if in fact the contractor sold substantial quantities of particular catalog items to the general public, thereby qualifying for a permissive exemption from the mandatory cost and pricing data submission and certification requirements imposed on negotiated procurements by 10 U.S.C. 2306(f), Public Law 87-653, the "Truth in Negotiation Act of 1962." In particular, you are interested in examining the manufacturer's sales records which pertain to the catalog sales exemption granted Electronic Associates, Inc. (EAI) of West Long Branch, New Jersey, by the cognizant contracting personnel at Marshall Space Flight Center, National Aeronautics and Space Administration (NASA) incident to the award of contracts number HAS8-15103 of June 30, 1965; HAS8-16789 of November 11, 1965; HAS8-17425 of February 10, 1966; and HAS8-17438 of May 6, 1966, for the purchase of electronic computers and associated equipment.

The letters attached to the July 10, 1967, memorandum show that procurement personnel at Marshall Space Flight Center, before award of the first above mentioned contract, unsuccessfully attempted to obtain detailed sales data for the particular items being procured, in order to independently determine whether the items actually had been sold in large quantities to nongovernment users. In the absence of more comprehensive sales data, the contracting officer was forced to rely upon an overall figure which simply segregated total yearly sales to the Government for all EAI products from total sales to nongovernmental customers and determined on this basis that because EAI had made substantial sales to the public, the contracts could be exempted from the cost certification requirements incident to negotiated procurements.

Under 10 U.S.C. 2313(b) the gist of which was included as paragraph 10(a) of the standard provision of the contracts in question, presumably on Standard Form 32 (Supply Contract), June 1964 edition, representatives of this Office are entitled to:

> "*** examine any books, documents, papers, or records of the contractor, or any of his subcontractors, that directly pertain to, and involve transactions relating to the contract or subcontract."

Commercial sales records do not pertain to or involve transactions relating to government contracts, and we have no right of access thereto under 10 U.S.C. 2313(b).

As to the propriety of the action of NASA contracting personnel in permitting contracts to be negotiated solely on the basis of catalog prices without any showing of substantial sales of the item to the public, it appears that the NASA contracting personnel have violated the criterion established by paragraph 3-807-1(a) of the NASA Procurement Regulation, that catalog price purchases require:

> "* * * positive demonstration by convincing evidence to support the application of this exception. It is not enough that an item be listed in a catalog or price list, or be offered for sale to the general public, or be intended to become a commercial item, but tangible and substantial sales activity must be shown to result from such listing, offering, or intention. * * *"

We interpret this regulation as applying on an item by item basis.

R. F. KELLER

Acting Comptroller General
of the United States

Attachment

B-141683-O. M. June 5, 1968

TO: Mr. Edward Friedman, Procurement, Defense Division

FROM: Mr. Stephen P. Haycock, Assistant General Counsel

Your memorandum of May 9, 1968, raises a question concerning the authority of GAO to review contractors' records with respect to both Government and commercial work under the Defense Production Act, 1950. You state that in connection with a survey Defense Division has accumulated some evidence that contractors are in violation of the priorities system contemplated by the Defense Production Act, 1950, and the Business and Defense Services Administration (EDSA) regulations implementing it. The precise question involved is whether GAO has a right to review contractors' commercial records with respect to production scheduling and shipments of material either under the Examination of Records Clause (Clause 10 of Standard Form 32) or under the authority granted the EDSA under the Defense Production Act, 1950. We understand that Defense Division is interested only incidentally, if at all, in cost and pricing data for the negotiated contracts that may be involved.

In regard to GAO's right of access to records under the Defense Production Act it would appear that no provision of the Act itself grants GAO the right to examine a contractor's commercial records relating to production scheduling, shipments of material or the like. On the contrary, it appears that certain provisions of the Defense Production Act and other legislation militate against any such conclusion. See 50 U.S.C. App. 2155(e) and 2162(c). See also Executive Order 20480, August 14, 1953, set out as a note under 50 U.S.C. App. 2153 and the analysis set forth in a memorandum dated April 21, 1960 (B-141683), by Mr. Masterson to Mr. Ramsey.

With respect to the Examination of Records Clause set forth in Standard Form 32 which apparently is incorporated in the negotiated contracts involved, it would appear that the types of records sought cannot reasonably be considered as

"directly pertinent * * * records of the Contractor involving transactions related to this contract" (Underscoring supplied) [sic]. In B-162009-O.M., August 31, 1967, the Director, Civil Division, was advised that GAO did not have a right of access to a manufacturer's sales records which pertain to the catalog sales exception granted to a contractor pursuant to the "Truth in Negotiation Act of 1962". The present records sought are even more removed from the coverage of Clause 10 of S.F. 32 than were the sales records involved in B-162009-O.M. See, also, B-158349-O.M., April 13, 1966, where it was observed that Fairchild Camera's refusal to provide statistical information relating to the overall financial activities of its Space and Defense Systems Division (which was performing only Federal contracts) was not necessarily contrary to law and that nothing in the law requires a contractor to furnish GAO with listings of its Government contracts or their degree of completion. *A fortiori* it must be concluded that nothing in the law requires a contractor to furnish GAO with records relating to production scheduling and shipments of materials in its commercial business.

B 159896 (.07) October 22, 1970

TO: General Counsel

FROM: Director, DD—C. M. Bailey

SUBJECT: Draft legislation expanding GAO's authority to perform "should cost" type reviews

In your decision, B-159896-O.M., dated September 8, 1970, you advised us that GAO apparently lacks firm statutory authority to perform comprehensive reviews of contractors' operations ("should cost" reviews). In our forthcoming report to the Congress, we intend to point this fact out and to suggest that the Congress may wish to consider expanding our authority in this area.

We believe it would be desirable for us to be prepared when the report is issued to the Congress, about January 31, 1971, with draft legislation that can be considered by appropriate committees. In our opinion, the proposed legislation should provide, as a minimum that:

1. Any contractor holding negotiated contracts valued at $100,000 or more will be subject to review.

2. GAO will have the right to examine into all aspects of operations and management, including but not limited to:

a. production systems and controls

b. plant design

c. labor standards

d. quality control systems

e. equipment utilization

f. indirect costs and controls

g. accounting and cost estimating systems

h. purchasing and subcontracting procedures

i. internal management studies and reviews

3. GAO's rights shall not be limited to documents and records pertinent to particular contracts, but should be broadly interpreted to permit access to all documents, records, personnel, and other data considered necessary to evaluate the efficiency and economy of the contractors' operations.

It would appear to be desirable for these rights to be incorporated into applicable Government contracts and the legislation could, therefore, be drafted so as to amend or replace the current contractual provisions for GAO access to contractors' records.

We would appreciate your drafting legislation to accomplish the objectives described above. Mr. Jerome H. Stolarow, Assistant Director of this Division, is responsible for our "should cost" review efforts and will be available to assist you if further information is needed.